

***United States Court of Appeals
for the Second Circuit***



**PETITION FOR
REHEARING
EN BANC**

77-6034,

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

Nos.

77-6034, 77-6038, 77-6045, 77-6048, 77-6065

In re

WEIS SECURITIES, INC.,

Debtor.

GEORGE D. ALDRICH, et al.,

Appellants,

v.

EDWARD S. REDINGTON, Trustee,
and SECURITIES INVESTOR
PROTECTION CORPORATION,

Appellees.

Appeal from the United States
District Court for the
Southern District of New York

PETITION FOR REHEARING AND SUGGESTION
FOR REHEARING IN BANC

(Counsel For Petitioners
Listed on Last Page of Petition)



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PRELIMINARY STATEMENT

The undersigned parties (the "Petitioners"), appellants in this appeal, hereby petition the Court pursuant to Rule 40 of the Federal Rules of Appellate Procedure to rehear this appeal and reconsider its judgment entered on June 12, 1978 and suggest pursuant to Rule 35 that it would be appropriate to have a rehearing in banc because of the importance of the issues raised in this appeal.

STATEMENT OF THE CASE

This Court's opinion filed on June 12, 1978 affirmed the judgment entered by Judge Wyatt in the Southern District of New York holding that claims of certain subordinated lenders, including Petitioners, to the estate of a broker-dealer now in liquidation should be enforced in accordance with the subordination agreements regardless of whether the subordination agreements were fraudulently procured or whether customers of the broker-dealer could show reliance on the subordination agreements. This Court stated the scope of its holding as follows:

[W]e agree with Judge Wyatt that customers of Weis need not show reliance on the subordination agreements to prevent rescission by the lenders. Since the remaining assets of Weis will be exhausted after satisfaction of the customers' claims, it is unnecessary to reach the question whether general creditors must prove reliance in order to prevent rescission. (Op. at 6) (Emphasis in original)

ARGUMENT

Petitioners respectfully submit that the Court's holding overlooked the following points: (1) the Court erred in assuming that satisfaction of the remaining customer claims would exhaust the assets in Weis' general estate; (2) the Court failed to recognize that the primary beneficiary of its holding would be the Securities Investor Protection Corporation ("SIPC") rather than customers of Weis; and (3) the Court disregarded the provisions of the Securities Investor Protection Act ("SIPA"), 15 U.S.C. §§78aaa-78lll, which govern the distribution of the assets contained in the general estate of a bankrupt broker-dealer. Each of these points will be discussed briefly below.

I. The Court Erred in Assuming that Satisfaction of the Remaining Customer Claims Would Exhaust the Assets in Weis' General Estate.

The claims of the vast majority of Weis' customers have been paid in full, and remaining unsatisfied customer claims total less than \$1 million. (Appellees' Br. at 29) There is nothing in the record to suggest that the general estate of Weis is smaller than \$1 million. Indeed, Petitioners understand from the Trustee's latest Progress Report that the Weis general estate is many times that size. Therefore, contrary to the Court's statement quoted above, it is entirely feasible to pay the remaining unsatisfied customer claims in full from the assets of Weis' general estate (or even from that portion of such assets which would be allocated to the subordinated lenders if they were permitted to rescind) and still have sufficient assets remaining to make a distribution to the subordinated lenders.

Moreover, there is an excellent possibility that the Weis general estate will become substantially larger. This Court recently reversed an order of the District Court dismissing the complaint of the Trustee and SIPC against Weis' auditors. Redington v. Touche Ross & Co., [Current Binder] Fed. Sec. L. Rep. (CCH) ¶96,404 (2d Cir. 1978). Accordingly, the Trustee and SIPC will be able to pursue their combined claim of \$65 million against Touche Ross & Co. Since the instant appeal is from an order of the District Court granting summary judgment against Petitioners, it would be improper to affirm such order based on factual assumptions which are not presently correct or which may become incorrect.

II. The Court Failed to Recognize that SIPC, Rather than Customers of Weis, Would be the Primary Beneficiary of its Holding.

Although the Court based its holding on "legislative solicitude for the interests of customers" (Op. at 8), the Court's opinion nowhere recognized that customers of Weis would not be the primary beneficiaries of its holding. Instead, with its subrogation claims of some \$13 million (Appellees' Br. at 29), SIPC stands to collect more than 13 times as much as a result of the Court's holding than do the public customers with unpaid claims. Yet SIPC is entitled to no more protection by this Court than are the admittedly innocent Petitioners who were fraudulently induced to execute subordination agreements. In enacting SIPA, Congress established a system of industry self-insurance to pay customer claims from the SIPC insurance fund which is financed by contributions from brokerage firms. 15 U.S.C. §78ddd. Realizing that SIPC would suffer losses because of its inability to recover all of the funds which it advanced to pay customer claims, Congress provided for the replenishment of the SIPC insurance fund through additional assessments on the brokerage firms which compose SIPC's membership. 15 U.S.C. §78ddd(c). In this way, the brokerage industry itself, through SIPC, was intended to bear part of the loss resulting from broker-dealer insolvencies. (Appellants' Br. at 8-9)

III. The Court Disregarded the Provisions of SIPA which Govern the Distribution of Assets in Weis' General Estate.

Congress demonstrated its "legislative solicitude

for the interests of customers" by enacting SIPA, which provides customers with two types of financial protection in the event of insolvencies. First, customers are entitled to receive from the SIPC insurance fund prompt payment of their claims up to \$50,000 against a broker-dealer in liquidation under SIPA without regard to whether the assets of the broker-dealer will be sufficient to reimburse such payments. 15 U.S.C. §78fff(f). Second, customers of a broker-dealer receive priority over general creditors with respect to the "single and separate fund" established under SIPA, which consists of all property which the broker-dealer held for the account of customers. 15 U.S.C. §78fff(c)(2). The remaining assets of a bankrupt broker-dealer are placed in its general estate. With respect to those assets, however, customer claims have no priority over the claims of other creditors under SIPA. Moreover, no provision of SIPA abrogates the right of defrauded lenders under the federal securities laws to rescind their subordination agreements. (Appellants' Br. at 11-19, 32-34) Therefore, the distribution scheme under SIPA provides for a pro rata sharing of the assets in Weis' general estate among all general creditors, including customer claims unsatisfied by payments from the SIPC insurance fund or from the "single and separate fund" and also including the claims of Petitioners after rescission of their subordination agreements.

CONCLUSION

For all the reasons stated above and in the previously filed briefs of appellants, it was neither necessary nor appropriate for the Court to take the extreme position that innocent

parties should be deprived of their statutory and common law right to rescind fraudulently induced agreements in order to protect the interests of Weis' customers or to preserve confidence in the regulatory scheme. Petitioners therefore request a rehearing of this appeal and suggest that a rehearing in banc would be appropriate.

Dated: June 26, 1978.

Respectfully submitted,

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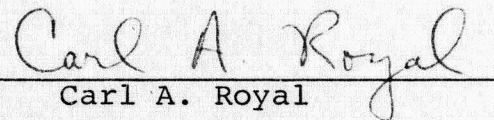
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UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

In the Matter of Weis	)	
Securities, Inc.,	)	
	)	
Debtor.	)	
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George Aldrich, et al.,	)	
	)	
Appellants,	)	
	)	
v.	)	
	)	
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and Securities Investor	)	77-6034
Protection Corporation,	)	77-6038
	)	77-6045
	)	77-6048
	)	77-6065
Appellees.	)	
-----	)	

CERTIFICATE OF SERVICE

The undersigned hereby certifies that he served the enclosed Petition for Rehearing and Suggestion for Rehearing in Banc by mailing two copies of the petition by first class mail, postage prepaid, to each of the persons named, at the addresses indicated, on the attached list on June 24, 1978.


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STATE OF NEW YORK, COUNTY OF

ss.:

The undersigned, an attorney admitted to practice in the courts of New York State,

Check Applicable Box

- ☐ Certification
By Attorney
- ☐ Attorney's
Affirmation

certifies that the within
has been compared by the undersigned with the original and found to be a true and complete copy.

shows: deponent is

the attorney(s) of record for
in the within action; deponent has read the foregoing
and knows the contents thereof; the same is
true to deponent's own knowledge, except as to the matters therein stated to be alleged on information and belief,
and that as to those matters deponent believes it to be true. This verification is made by deponent and not by

The grounds of deponent's belief as to all matters not stated upon deponent's knowledge are as follows:

The undersigned affirms that the foregoing statements are true, under the penalties of perjury.

Dated:

.....
The name signed must be printed beneath

STATE OF NEW YORK, COUNTY OF

ss.:

Check Applicable Box

- ☐ Individual
Verification
- ☐ Corporate
Verification

the
the foregoing
deponent's own knowledge, except as to the matters therein stated to be alleged on information and belief, and as
to those matters deponent believes it to be true.

the
a
foregoing
is true to deponent's own knowledge, except as to the matters therein stated to be alleged upon information and
belief, and as to those matters deponent believes it to be true. This verification is made by deponent because
is a corporation and deponent is an officer thereof.

The grounds of deponent's belief as to all matters not stated upon deponent's knowledge are as follows:

Sworn to before me on

19

.....
The name signed must be printed beneath

STATE OF NEW YORK, COUNTY OF

ss.:

is over 18 years of age and resides at

being duly sworn, deposes and says: deponent is not a party to the action,

Check Applicable Box

- ☐ Affidavit
of Service
By Mail
- ☐ Affidavit
of Personal
Service

On 19 deponent served the within
upon
attorney(s) for in this action, at

the address designated by said attorney(s) for that purpose
by depositing a true copy of same enclosed in a post-paid properly addressed wrapper, in — a post office — official
depository under the exclusive care and custody of the United States Postal Service within the State of New York.

On 19 at upon
deponent served the within

herein, by delivering a true copy thereof to h personally. Deponent knew the
person so served to be the person mentioned and described in said papers as the therein.

Sworn to before me on

19

.....
The name signed must be printed beneath

NOTICE OF ENTRY

Index No.

77-6034

Year 19

Sir:- Please take notice that the within is a (certified)
true copy of a
duly entered in the office of the clerk of the within
named court on 19

Dated,

Yours, etc.,

Attorney for

Office and Post Office Address

To

Attorney(s) for

NOTICE OF SETTLEMENT

Sir:- Please take notice that an order

of which the within is a true copy will be presented
for settlement to the Hon.

one of the judges of the within named Court, at

on the day of 19
at M.

Dated,

Yours, etc.,

Attorney for

Office and Post Office Address

To

Attorney(s) for

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

IN THE MATTER OF WEIS
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v.

~~EDWARD S. REDINGTON, TRUSTEE~~, and et ano:

CERTIFICATE OF SERVICE

WINICK & SHERMET, P.C.

Attorney for APPELLANTS

Office and Post Office Address, Telephone

500 Fifth Avenue
New York, New York 10036

To

Attorney(s) for

Service of a copy of the within

is hereby admitted.

Dated,

Attorney(s) for